(3)

No. 09-865

Supreme Court, U.S.
FILED
MAR 9 - 2009
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

MONUMENTAL LIFE INSURANCE COMPANY
(Successor in interest to COMMONWEALTH LIFE INSURANCE COMPANY),

Petitioner,

v.

DEPARTMENT OF REVENUE, FINANCE AND ADMINISTRATION CABINET, COMMONWEALTH OF KENTUCKY (f/k/a Revenue Cabinet); LOUISVILLE/JEFFERSON COUNTY METRO GOVERNMENT (f/k/a Jefferson County, Kentucky and the City of Louisville, Kentucky); and KENTUCKY BOARD OF TAX APPEALS,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE KENTUCKY COURT OF APPEALS

REPLY BRIEF

WILLIAM A. CHITTENDEN, III
JULIE F. WALL
CHITTENDEN, MURDAY & NOVOTNY LLC
303 West Madison Street
Suite 1400
Chicago, IL 60606
(312) 281-3601

MARK F. SOMMER
Counsel of Record
MARK A. LOYD
GREENEBAUM DOLL & McDONALD PLLC
3500 National City Tower
101 South Fifth Street
Louisville, KY 40602-3197
(502) 587-3570
MFS@gdm.com

Counsel for Petitioner

228654

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Petitioner's corporate disclosure statement was set forth at page *ii* of its Petition for a Writ of Certiorari, and there are no amendments to that statement.

TABLE OF CONTENTS

Page

RULE 29.6 CORPORATE DISCLOSURE STATEMENT i

TABLE OF CONTENTS ii

TABLE OF APPENDICES iv

TABLE OF CITED AUTHORITIES v

REPLY BRIEF FOR THE PETITIONER 1

A. ERISA Tax Preemption and the Effect of This Court's Decisions are Recurring Issues of Great Importance To Countless Retirement/Pension Plans, Their Fiduciaries, Retirees and Sponsoring Businesses 1

B. The ERISA Preemption Question Was Preserved and Warrants This Court's Time to Review and Resolve Conflicting Jurisprudence 3

1. Kentucky Cannot Bar This Court from Reviewing the ERISA Preemption Question Via an Erroneously Invoked and Unevenly Applied Procedural Rule 3

Contents

Page

2. Monumental Timely and Properly Presented the ERISA Preemption Question to the KBTA 6

3. ERISA Protects the Involved Plans, and Kentucky's Arguments Only Reinforce the Actual Conflict Between This Court's Opinions in *De Buono* vs. *Egelhoff* and Others, Particularly as to ERISA's "Connection With" Test 8

C. Kentucky Admits *St. Ledger* Applies to the KRS 136.320 Tax On Stock, and This Court's Precedents In *St. Ledger*, *Fulton* and Other Opinions Must Be Given Effect 10

1. From the Outset of this Litigation, Kentucky Has Recognized that *St. Ledger* Had a Controlling Effect on the KRS 136.320 Tax 11

2. Kentucky Has Recognized that Stock Is Considered in the Tax Computation When Treated as Exempt Which Implicates This Court's Precedent 13

CONCLUSION 14

TABLE OF APPENDICES

Page

APPENDIX A — FINAL RULING LETTER OF THE KENTUCKY REVENUE CABINET DATED JULY 21, 2000 ..... 1a

APPENDIX B — *CSX CORPORATION AND SUBSIDIARIES VS. DEPARTMENT OF REVENUE*, NO. K08-4-37 (KBTA) – ORDER ON MOTION FOR AND MEMO IN SUPPORT OF LIMITING THE KENTUCKY DEPARTMENT OF REVENUE TO FINAL RULING DATED JUNE 3, 2009 ..... 9a

APPENDIX C — ANNUAL STATEMENT ("BLUE BOOK") OF THE COMMONWEALTH LIFE INSURANCE COMPANY OF LOUISVILLE IN THE STATE OF KENTUCKY FOR THE YEAR ENDED DECEMBER 31, 2006 [SELECTED EXCERPTS – COVER PAGE AND PAGE 2 ONLY] 11a

TABLE OF CITED AUTHORITIES

Page

CASES

American Bank & Trust Co. v. Dallas County,
463 U.S. 855 (1983) 14

Baker v. Campbell County Bd. of Educ.,
180 S.W.3d 479-82 (Ky. App. 2005) 5

Campbell v. Louisiana,
523 U.S. 392 (1998) 8

Cornette v. Holiday,
32 S.W.3d 106 (Ky. App. 2000) 5

Cousins v. Wigoda,
419 U.S. 477 (1975) 5

CSX Corp. v. Dep't of Revenue,
No. K08-R-37, Order (unnumbered)
(KBTA 2009) 7

De Buono v. NYSA-ILA Medical & Clinical Services Fund,
520 U.S. 806 (1997) 8, 9

Egelhoff v. Egelhoff ex rel. Breiner,
532 U.S. 141 (2001) 8, 9

Ellis Race & Entm't Ctr., Inc. v. Revenue Cabinet,
1995 WL 107364 (KBTA 1995) 6, 7

Cited Authorities

	Page
Hathorn v. Lovorn, 457 U.S. 255 (1982)	3, 8
Hunt-Wesson v. California, 528 U.S. 458 (2000)	14
Jimmy Swaggart Ministries v. Board of Equalization, 493 U.S. 378 (1990)	5
Johnson v. Smith, 885 S.W.2d 944 (Ky. 1994)	5
Miller v. Johnson Controls, Inc., 296 S.W.3d 392 (Ky. 2009), *Petition for Certiorari filed*, No. 09-981 (U.S. Feb. 22, 2010)	2
National Life Insurance Co. v. United States, 227 U.S. 508 (1928)	13
Parents Involved in Community Schools v. Seattle School Dist. No. 1, 551 U.S. 701 (2007)	10
PruneYard Shopping Center v. Robins, 447 U.S. 74 (1980)	4, 8
Ready v. Jamison, 705 S.W.2d 479 (Ky. 1986)	5

Cited Authorities

Page

Revenue Cabinet v. Babcock & Wilcox Co.,
203 S.W.3d 149 (Ky. App. 2005) 7

Southside Real Estate Developers, Inc. v. Pike County Fiscal Court,
294 S.W.3d 453 (Ky. App. 2009) 5

St. Ledger v. Kentucky Revenue Cabinet,
517 U.S. 1206 (1996) ..... *passim*

Stoner Creek Stud, Inc. v. Revenue Cabinet,
746 S.W.2d 73 (Ky. App. 1987) 6

Street v. New York,
394 U.S. 576 (1969) 3, 8

STATUTES

29 U.S.C. § 1144 1

29 U.S.C. § 1144(a)&(b)(5)(B)(i) 9

Ky. Rev. Stat. § 136.030 12

Ky. Rev. Stat. § 131.340(1) 6

Ky. Rev. Stat. § 132.020(1) 11, 12

Ky. Rev. Stat. § 136.320 ..... *passim*

Cited Authorities

Page

Ky. Rev. Stat. § 136.320(1)(a) 13

Ky. Rev. Stat. § 136.320(2)(a) 11, 13

Ky. Rev. Stat. § 136.320(3) 11

Tenn. Code Ann. § 67-5-1205 2

Tex. Code Ann. § 1102 2

Rules

Ky. R. Civ. P. 76.12(4)(c) 4, 5

Other Authorities

Towers Watson, 2010 Global Pension Asset Study (Jan. 2010), *available at* http://www.towerswatson.com/assets/pdf/966/GPAS2010.pdf. 1

REPLY BRIEF FOR THE PETITIONER

This Petition presents two questions: [1] whether ERISA[1] preempts the imposition of Ky. Rev. Stat. ("KRS") 136.320 *ad valorem* tax on retirement/pension plan assets held in Separate Accounts; and, [2] whether Kentucky must follow and apply this Court's Order in *St. Ledger*[2] as well as precedent in other cases. Respectfully, for the reasons set forth this Court should grant review on each question.

A. ERISA Tax Preemption and the Effect of This Court's Decisions are Recurring Issues of Great Importance To Countless Retirement/Pension Plans, Their Fiduciaries, Retirees and Sponsoring Businesses

Ad valorem property taxes are a mainstay of state revenue. Transitioning from an agrarian/manufacturing based economy to one based more on service/intangible property [*e.g.*, $13.2 trillion in U.S. pension assets in 2009],[3] states looking for revenue have turned their "taxing" attention to these tax bases.

KRS 136.320 remains the law today, and as taxpayers must comply with it, it is axiomatic that it is worthy of

---

[1] 29 U.S.C. § 1144 ("ERISA").

[2] *St. Ledger v. Kentucky Revenue Cabinet*, 517 U.S. 1206 (1996) [See Pet. n. 3 for citation with full case history].

[3] *See* Towers Watson, 2010 Global Pension Asset Study (Jan. 2010), *available at* http://www.towerswatson.com/assets/pdf/966/GPAS2010.pdf.

this Court's focus. Under the Kentucky Court of Appeals' holding, the tax would continue to apply to ERISA-governed retirement/pension plan assets held in Separate Accounts. Other states have similar tax statutes. *See, e.g.*, Tenn. Code Ann. § 67-5-1205; Tex. Code Ann. § 11.02. Call it what they will, Kentucky is taxing pension assets – this violates ERISA.

The ERISA preemption question has been preserved for review by Petitioner ("Monumental"), though Respondents ("Kentucky") attempt to cast doubt. Kentucky's allusions to the contrary notwithstanding, the evidentiary record is indisputably clear that the Separate Accounts consist of retirement/pension plan assets and therefore, a compelling case for review is presented: whether ERISA preempts this state tax law applied to ERISA-governed plan assets because the tax has *an impermissible connection with* an employee benefit plan.

Moreover, the Brief in Opposition demonstrates Kentucky's repeated improper elevation of state law *over* federal law and this Court's decisions, including *St. Ledger*. *St. Ledger* did impact KRS 136.320 as confirmed by Kentucky itself in its Final Ruling. This Court's other precedent likewise applies. While this obviously does not concern Kentucky,[4] it should concern this Court.

Monumental respectfully disagrees with many of Kentucky's statements. For instance, though Kentucky

---

[4] *See, e.g., Miller v. Johnson Controls, Inc.*, 296 S.W.3d 392 (Ky. 2009), *Petition for Certiorari filed*, No. 09-981 (U.S. Feb. 22, 2010).

claims it was not aware of the existence of Separate Accounts prior to 1998 [Opp. 4-6], the evidence established that Kentucky was aware – for decades. Separate Accounts were identified in each of the annual Blue Books that Kentucky concedes Monumental provided to it. *See* Reply App. 11a (where 1996 "Separate Accounts" line 24, page 2 is *the largest single line item*, $1,596,179,388 of $4,750,301,268 (or 33.6%) of the total assets reported). Countless other examples exist.

B. The ERISA Preemption Question Was Preserved and Warrants This Court's Time to Review and Resolve Conflicting Jurisprudence

"The issue [of] whether a federal question was sufficiently and properly raised in the state courts is itself ultimately a federal question, as to which this Court is not bound by the decision of the state courts." *Street v. New York*, 394 U.S. 576, 583-85 (1969). Kentucky has it backwards in its Brief. Opp. 7.

1. Kentucky Cannot Bar This Court from Reviewing the ERISA Preemption Question Via an Erroneously Invoked and Unevenly Applied Procedural Rule

"State courts may not avoid deciding federal issues by invoking procedural rules that they do not apply evenhandedly to all similar claims." *Hathorn v. Lovorn*, 457 U.S. 255, 262-65 (1982). Monumental preserved the ERISA preemption question for this Court's review

under this Court's rules for preserving a challenge to a state law repugnant to federal law:

> It is well settled that in challenging the validity of a state law on the ground that it is repugnant to the Constitution of the United States, "[n]o particular form of words or phrases is essential, but only that the claim of invalidity on the ground therefor be brought to the attention of the state court with fair precision and in due time. And if the record as a whole shows either expressly or by clear intendment that this was done, the claim is to be regarded as having been adequately presented."

PruneYard Shopping Center v. Robins, 447 U.S. 74, 85, n. 9 (1980) (citations omitted).

Analysis begins with the Court of Appeals stating, "Monumental does not cite us to its preservation of this issue as required by CR 76.12(4)(c)," then considering quotes by the Kentucky Board of Tax Appeals ("KBTA") which stated that it would "not consider the ERISA issue" (though the KBTA ultimately ruled on the ERISA preemption question on the merits) [Pet. App. 64a], further stating, "As we have otherwise not been cited to Monumental's proper preservation of the issue, we will likewise not address this argument on the merits." Pet. App. 24a (citations omitted).

Kentucky Rule of Civil Procedure ("CR") 76.12(4)(c) requires "a statement with reference to the record showing whether the issue was properly preserved for

review and, if so, in what manner." Kentucky's Civil Rules, including CR 76.12(4)(c), are *not strictly construed*, and dismissal (the effect of not hearing a question on the merits) is disfavored. *See Ready v. Jamison*, 705 S.W.2d 479, 481-82 (Ky. 1986); *Cornette v. Holiday*, 32 S.W.3d 106, 109 (Ky. App. 2000); *Johnson v. Smith*, 885 S.W.2d 944, 950 (Ky. 1994).

The Court of Appeals routinely decides issues on the merits without a CR 76.12(4)(c) statement, for example, when (as here) the issue was clearly joined at every stage [*Cornette*, 32 S.W.3d at 109; *Baker v. Campbell County Bd. of Educ.*, 180 S.W.3d 479-82 (Ky. App. 2005)] or to "avert a manifest injustice" [*Southside Real Estate Developers, Inc. v. Pike County Fiscal Court*, 294 S.W.3d 453, 457 (Ky. App. 2009) (quotation omitted)]. And, demonstrating *per se* inconsistent application herein – in *Southside* the Court *addressed a federal preemption question* in the absence of a CR 76.12(4)(c) statement. *Id.*

The Court of Appeals has *routinely ignored* the CR 76.12(4)(c) statement – *but inexplicably not here* – even though Monumental raised a federal ERISA preemption question *and* briefed and defended it at every stage, *i.e.*, KBTA, Circuit Court and Court of Appeals. Thus, unlike the ruling State Courts in *Jimmy Swaggart Ministries v. Board of Equalization*, 493 U.S. 378, 397-99 (1990) and *Cousins v. Wigoda*, 419 U.S. 477, 486-87 (1975) [Opp. 12-13], the Court of Appeals' refusal to address ERISA preemption under a procedural rule was in error, unevenly applied and inherently prejudicial to Monumental.

2. Monumental Timely and Properly Presented the ERISA Preemption Question to the KBTA

Monumental presented the ERISA preemption question under KBTA rules and practice by appealing the taxation of Separate Accounts *issue* and making the ERISA preemption *argument* to the KBTA.

KRS 131.340(1) governs a *de novo* appeal from a Final Ruling: "The [KBTA] is . . . vested with exclusive jurisdiction to hear and determine appeals from final rulings . . . of any agency of state...government affecting . . . taxation. [KBTA] [a]dministrative hearings...shall be de novo. . . ." In a KBTA appeal, an "issue" has a particular meaning. *Stoner Creek Stud, Inc. v. Revenue Cabinet*, 746 S.W.2d 73, 77 (Ky. App. 1987), for example, upheld the KBTA's refusal to address the "issues" of the taxability of motor fuels and catalog purchases though the KBTA addressed others. *Id.* at 74-77. Obviously, an "issue" is an item, the taxability of which is questioned in a Final Ruling, *e.g.*, motor fuels, catalog purchases, etc.

An "issue" can encompass multiple "arguments." For example, post-*Stoner Creek*, in *Ellis Race & Entm't Ctr., Inc. v. Revenue Cabinet*, 1995 WL 107364 (KBTA 1995), regarding the *issue* of the taxability of certain sales, the KBTA considered several "argument[s]" including federal due process and equal protection challenges, "constitutional provisions that [Ellis] had not previously

cited in its . . . petition of appeal or . . . prehearing order." Thus, in *Ellis*, the KBTA rejected a "strict waiver theory."[5]

Here, Respondent Kentucky Department of Revenue issued a Final Ruling to Monumental ("Kentucky's Final Ruling"), designating "Separate Accounts" as an "*issue*" in dispute: "***At issue*** concerning the assessments . . . of the . . . tax imposed by KRS 136.320 is the propriety of assessing . . . separate accounts." Reply App. 6a (emphasis added).

Monumental appealed the Separate Accounts "issue" in its KBTA Petition of Appeal in the "Issues" section: ". . . [T]his action involves . . . another . . . issue: whether . . ."Separate Account Statement" assets and reserves are included within the computation of Capital Stock Tax levied pursuant to KRS 136.320." Monumental also set forth its position, *i.e.*, that they are not. This met the KBTA's requirements for a Petition of Appeal.[6]

When a taxpayer preserves an issue (*i.e.*, Separate Accounts' taxability) in its KBTA Petition of Appeal as Monumental did, that taxpayer may then advance

---

[5] *See also Revenue Cabinet v. Babcock & Wilcox Co.*, 203 S.W.3d 149, 155 (Ky. App. 2005) (holding that the issue of an account's taxability was properly before the KBTA); *CSX Corp. v. Dep't of Revenue*, No. K08-R-37, Order (unnumbered) (KBTA 2009) [Reply App. 9a-10a].

[6] Notably, 802 KAR 1:010, as in effect when this case was before the KBTA, did not require a pre-hearing statement. Kentucky's Brief in Opposition at pages 9, 10 & 15 improperly cites from a later version of the KBTA's Regulation.

multiple arguments (*e.g.*, ERISA preemption) on brief in support thereof. Thus, in contrast to the Petitioner in *Campbell v. Louisiana*, 523 U.S. 392, 403 (1998), cited by Kentucky. Monumental has met its burden of showing that the federal question (here, ERISA preemption) was adequately presented to the KBTA and to the Kentucky Court of Appeals so that this Court may review it. *See Street, supra; Hathorn, supra; Prune Yard, supra.*

3. ERISA Protects the Involved Plans, and Kentucky's Arguments Only Reinforce the Actual Conflict Between This Court's Opinions in *De Buono* vs. *Egelhoff* and Others, Particularly as to ERISA's "Connection With" Test

The Court of Appeals held that, "The separate account assets consist principally of retirement fund amounts held for distribution to retirees in the future." Pet. App. 20a. It is unfortunate that Kentucky now suggests that the record does not support the nature of the Separate Accounts, though Kentucky failed to assert this before the Kentucky Supreme Court. Merely one of many possible cites is demonstrative: Professor Richard D. Pomp testifying as an expert stated, "I think they [referring to the Separate Accounts] are covered by the pre-emption language in ERISA."[7]

---

[7] The record overwhelmingly supports the Petitioner; multiple witnesses offered unrefuted testimony as to the nature of the Separate Accounts assets, including employees of Kentucky.

ERISA's express text evidences Congress' intent to preempt state tax laws that relate to employee benefit plans such as the Separate Accounts. *See* 29 U.S.C. § 1144(a)&(b)(5)(B)(i). Though citing it and other cases, Kentucky emphasizes *De Buono v. NYSA-ILA Medical & Clinical Services Fund*, 520 U.S. 806, 809 (1997), which held that ERISA did not preempt New York's gross receipts tax on the income of medical centers operated by ERISA funds. Opp. 17-18. *De Buono* gave little weight to Congress' preemptive intent in ERISA's text [*De Buono*, 520 U.S. at 815 n. 11], and Kentucky reads *De Buono* to create a virtually *per se* unrebuttable presumption against preemption of a general tax – this is not the law.

One conflict presented is that *De Buono* predates this Court's decision in *Egelhoff v. Egelhoff ex rel. Breiner*, 532 U.S. 141 (2001), which confirmed that ERISA preempts general laws having an "impermissible connection with" an employee benefit plan and made clear, "[T]hat presumption can be overcome where, as here, Congress has made clear its desire for preemption." *Id.* at 143, 147-52 (and legislative history discussed therein). Moreover, Kentucky has not disputed the multiple and significant connections (including state tax lien, personal liability, and licensure provisions) between the *ad valorem* tax at issue and the involved Separate Account retirement assets. *Compare*, Pet. 27-29, *with* Opp. 16-24.

In the nearly 36 years since ERISA's enactment, it is believed that this Court has opined only twice on ERISA preemption in the context of state and local taxes. The last time was in *De Buono* in 1997; the case

law has since evolved. Imposing *ad valorem* state and local tax on Separate Accounts consisting of ERISA-governed retirement/pension plan assets presents an ideal and needed vehicle for this Court to clarify its jurisprudence as to the preemptive effect of ERISA's text to general state and local taxes.

C. Kentucky Admits *St. Ledger* Applies to the KRS 136.320 Tax On Stock, and This Court's Precedents In *St. Ledger*, *Fulton* and Other Opinions Must Be Given Effect

"Law is not an exercise in mathematical logic." *Parents Involved in Community Schools v. Seattle School Dist. No. 1*, 551 U.S. 701, 831 (2007) (J. Breyer dissenting). Kentucky's ten pages of mind numbing permutations of tautological computations simply do not add up.[8] The "math" here does not control here any more than it did in *Fulton Corp.*, cited by this Court in *St. Ledger* in remanding this case back to the Kentucky Supreme Court [*St. Ledger*, 517 U.S. at 1206]. The converse is true – the law controls the math. Thus, the proper approach here is not to allow some contrived and unproven mathematical theorem to control the result, but rather for this Court's Order in *St. Ledger* to dictate how to compute the tax of KRS 136.320 [Pet. App. 82a-84a].

Kentucky's mathematical theory is flawed as Judge Thompson recognized in his dissent. Pet. App. 32a-33a.

---

[8] And tellingly, Judge Thompson suggested at one of the two Court of Appeals' oral arguments herein that even he, a math major in college, did not follow Kentucky's theory.

Tax on stock valued at $234,401,794 is $1,640,813 (using the $0.70 per $100 rate for taxable capital [KRS 136.320(3)]), which is much closer to the tax resulting from "excluding" stock [$1,562,285], versus treating stock as "exempt" [$144,462] in the computation. *Compare with* Opp. 27 & 30. Again, law controls the math.

1. From the Outset of this Litigation, Kentucky Has Recognized that *St. Ledger* Had a Controlling Effect on the KRS 136.320 Tax

St. Ledger applied to the KRS 136.320 tax on stock, contrary to Kentucky's representations in its Brief in Opposition. Suggestions to the contrary are simply inaccurate. In 2000, Kentucky ruled [Reply App. 1a-4a]:

> At issue . . . is the application of the Commerce Clause principle of nondiscrimination against interstate commerce recognized and applied in *St. Ledger v. Revenue Cabinet.*
>
> * * *
>
> The . . . language [of KRS 136.320(2)(a)] is virtually indistinguishable from the language in KRS 132.020(1) levying the general intangible property tax, which was implicated in *St. Ledger.* . . .
>
> Included in the "company's intangible personal property exempt from taxation by law" or "exempt intangible personal

> property" is stock exempted under KRS 136.030, another statute whose constitutionality was at issue in *St. Ledger*. See KRS 136.320(1)(b) and (2)(a). . . .
>
> * * *
>
> Thus, KRS 136.320's utilization of KRS 136.030 in its computation of "taxable capital" rendered it violative of the United States Constitution's Commerce Clause in the same manner as KRS 132.020(1) and 136.030 were held in *St. Ledger* to contravene that constitutional provision.

(citations omitted).

St. Ledger had an effect on KRS 136.320; Kentucky admits this. On remand from this Court, the approach Kentucky selected to remedy the *St. Ledger* constitutional infirmity was to strike down both the exemption statute KRS 136.030[9] and the tax on stock in KRS 132.020(1).

Here, the Court of Appeals did not apply the remedy Kentucky selected for this particular constitutional infirmity, *i.e.*, striking "shares of stock" from the tax (KRS 136.320) statute [Monumental's position]; instead, its Opinion leaves the tax on stock intact and treats stock as exempt intangible personal property [Kentucky's

---

[9] KRS 136.030 was in effect at all times during the underlying tax years involved herein, but was repealed effective January 1, 2006.

position]. Pet. App. 16a-17a. Kentucky's position is in clear conflict with *St. Ledger* and *Fulton*.

2. Kentucky Has Recognized that Stock Is Considered in the Tax Computation When Treated as Exempt Which Implicates This Court's Precedent

Kentucky erroneously suggests that *St. Ledger* is not controlling herein and should not be followed; to the contrary, Kentucky ruled that treating stock as exempt intangible personal property *requires* stock to be "considered" in the KRS 136.320 tax computation:

> [Kentucky] has based its calculation of the refunds due the taxpayer [Monumental] on an approach that ***retains stock in the computation*** of "capital" under KRS 136.320(1)(a) ***but later exempts all of it*** as "intangible personal property exempt from taxation by law" in arriving at "taxable capital." KRS 136.320(2)(a).

[Reply App. 4a] ([ ] and emphasis added).

KRS 136.320's tax computation, even when applying Kentucky's own words, "considers" shares of stock when it is treated as exempt intangible personal property and violates this Court's clear rules against taxing indirectly that which cannot be taxed directly; "consideration" of an item (*e.g.*, whether federal obligations, or here, stock) in a tax computation, directly or indirectly, effectively subjects it to tax as held by this Court. *See National Life Insurance Co. v. United States*, 227 U.S. 508 (1928);

American Bank & Trust Co. v. Dallas County, 463 U.S. 855 (1983); *Hunt-Wesson v. California*, 528 U.S. 458 (2000).

CONCLUSION

For the foregoing reasons and those stated in the Petition for a Writ of Certiorari, the Petition for a Writ of Certiorari should be granted and this action heard.[10]

Respectfully submitted,

MARK F. SOMMER
Counsel of Record
MARK A. LOYD
GREENEBAUM DOLL & McDONALD PLLC
3500 National City Tower
101 South Fifth Street
Louisville, KY 40602-3197
(502) 587-3570
MFS@gdm.com

WILLIAM A. CHITTENDEN, III
JULIE F. WALI
CHITTENDEN, MURDAY & NOVOTNY LLC
303 West Madison Street
Suite 1400
Chicago, IL 60606
(312) 281-3601

Counsel for Petitioner

[10] Alternatively, this Court should issue a "Grant, Vacate and Remand" Order.

APPENDIX

APPENDIX A — FINAL RULING LETTER OF THE KENTUCKY REVENUE CABINET DATED JULY 21, 2000

REVENUE CABINET
DEPARTMENT OF LAW
200 FAIR OAKS LANE
FRANKFORT, KENTUCKY 40620

July 21, 2000

Commonwealth Life Insurance Co./
Monumental Life Insurance Co.
C/O Aegon USA, Inc.
4333 Edgewood Road NE
Cedar Rapids, IA 52499

Gentlemen:

Commonwealth Life Insurance Company, also known as Monumental Life Insurance Company, hereinafter referred to as "Commonwealth" or taxpayer, has outstanding refund claims of state taxes paid pursuant to KRS 136.320 for the years 1990 through 1996 in the amount of $6,751,758.46 (plus applicable interest). In addition, Commonwealth has outstanding assessments of the state tax imposed by KRS 136.320 for the years 1995 through 1998 in the amount of $4,108,444.52 (plus applicable penalty and interest).

At issue with respect to the refund claims is the application of the Commerce Clause principle of nondiscrimination against interstate commerce recognized and applied in *St Ledger v. Revenue Cabinet*,

Ky., 912 S.W.2d 34 (1995), *cert. granted, judgment vacated and case remanded*, 517 U.S. 1206, 116 S.Ct. 1821, 134 L.Ed.2d 927, (1996), *on remand*, Ky., 942 S.W.2d 893 (1997), *cert. dism'd*, 521 U.S. 1146, 118 S.Ct. 27, 138 L.Ed.2d 1057 (1997).

Commonwealth is (or was) a life insurance company incorporated under the laws of and doing business in Kentucky as of January 1 of the years to which the refund claims at issue relate. KRS 136.320(1). It therefore was properly subject to the annual taxes on "taxable capital" that are imposed or authorized by KRS 136.320 for state, county and city purposes. KRS 136.320(1), (3), (4) and (5).

""Taxable capital' [is] determined by deducting 'taxable reserves' from 'capital,' less exempt intangible personal property." KRS 136.320(2)(a) "Capital" for purposes of this calculation is defined as follows:

> The fair cash value of the company's intangible personal property, hereinafter referred to as "capital," consisting of all money in hand, shares of stock, notes, bonds, accounts, and other credits, exclusive of due and deferred premiums, whether secured by mortgage, pledge, or otherwise, or unsecured.

The foregoing language is virtually indistinguishable from the language in KRS 132.020(1) levying the general intangible property tax, which was implicated in *St. Ledger*. *See St. Ledger v. Commonwealth*, Ky., 912 S.W.2d 34, 37, 39 (1995).

Appendix A

Included in the "company's intangible personal property exempt from taxation by law" or "exempt intangible personal property" is stock exempted under KRS 136.030, another statute whose constitutionality was at issue in *St. Ledger*. See KRS 136.320(1)(b) and (2)(a). Subsection 1 of KRS 136.030 states:

> The individual stockholders of a corporation shall not be required to list their shares for ad valorem taxation so long as the corporation pays taxes to the State of Kentucky on at least seventy-five percent (75%) of its total property, wherever located. Bonds and obligations of the United States of America and its possessions and bonds and obligations of the State of Kentucky, its instrumentalities, and its political subdivisions and their instrumentalities shall not be considered in the computation of the total property of the corporation, wherever located, nor in the computation of the amount of property upon which the corporation pays ad valorem taxes to the State of Kentucky. In order to obtain this exemption, the stockholder shall furnish satisfactory proof to the Revenue Cabinet that at least seventy-five percent (75%) of the total property of the corporation as hereinabove specified is taxed in the State of Kentucky.

Thus, KRS 136.320's utilization of KRS 136.030 in its computation of "taxable capital" rendered it violative of the United States Constitution's Commerce Clause

in the same manner as KRS 132.020(1) and 136.030 were held in *St. Ledger* to contravene that constitutional provision. That is, the provisions in question discriminated against interstate commerce by providing a direct commercial advantage to local business. This was accomplished by KRS 136.030's allowing an exemption to corporations "pay[ing] taxes to the State of Kentucky on at least seventy-five percent (75%) of its total property, wherever located" while denying an exemption to other corporations.

Commonwealth relies upon the *St. Ledger* decision to argue that its stock should be removed or excluded from the threshold computation of "capital" in KRS 136.320(1)(a). In other words, it would strike the word "stock" from KRS 136.320(1)(a) to exclude stock at the outset of the computation, thereby making it unnecessary to exempt it later on in the computation of "intangible personal property exempt from taxation by law." KRS 136.320(1)(b) and (2)(a). The Cabinet has based its calculation of the refunds due the taxpayer on an approach that retains stock in the computation of "capital" under KRS 136.320(1)(a), but later exempts all of it as "intangible personal property exempt from taxation by law" in arriving at "taxable capital." KRS 136.320(2)(a).

The Cabinet has already issued Commonwealth refunds for the years in question (1990 through 1996) in accordance with its approach as outlined in the immediately preceding paragraph. The amount of the outstanding refund claims stated in the very first

paragraph of this final ruling represents the additional amount Commonwealth contends is due it based upon its approach, which is also outlined above in the immediately preceding paragraph.

It is the Cabinet's position that its approach is the proper one in this situation. First, its approach comports with the Commerce Clause mandate, recognized and applied in *St. Ledger,* of equal treatment of, and nondiscrimination between, interstate and intrastate commerce. Commonwealth's approach goes far beyond what is necessary to redress any constitutional violation to grant itself a tax windfall. "It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing business." *Western Life Stock v. Bureau of Revenue*, 303 U.S. 250, 254, 58 S.Ct. 546, 548, 82 L.Ed. 823 (1938).

Second, it is well settled that a cardinal principle of statutory construction is to save and not destroy. No more of a statute should be invalidated than is necessary to rectify a constitutional infirmity. in this situation, the only language that needs to be stricken to remedy the constitutional violation is the language in KRS 136.030(1) that follows "The individual stockholders of a corporation shall not be required to list their shares for ad valorem taxation."

It should also be noted that interest is not payable on any refund based upon the invalidity of KRS 136.320 that may be determined to be due in this proceeding.

See Revenue Cabinet v. St. Ledger, Ky. App., 955 S.W.2d 539, 544 (1997).

At issue concerning the assessments outstanding to Commonwealth of the state tax imposed by KRS 136.320 is the propriety of assessing what Commonwealth refers to as separate accounts. These accounts clearly include items that are capital within the meaning of KRS 136.320(1)(a) and should have been reported as such. Commonwealth's omission of these accounts from its report of capital pursuant to KRS 136.320 rendered it properly assessable by the Cabinet. There is ample authority for this action. *See, e.g.* KRS 136.320; 131.110; 131.130; 132.290; 132.320.

Based on the above, it is the position of the Cabinet that Commonwealth's outstanding refund claims have been properly denied and that the assessments outstanding (plus applicable penalty and interest) to the Commonwealth of Kentucky are properly due and owing.

This letter is the final ruling of the Revenue Cabinet.

You may appeal this ruling to the Kentucky Board of Tax Appeals pursuant to the provisions of KRS 131.110, KRS 131.340-131.365, 103 KAR 1:010 and 802 KAR 1:010. If you decide to appeal this ruling, you must file your complaint or petition of appeal with the Clerk, Kentucky Board of Tax Appeals, 128 Brighton Park Boulevard, Frankfort, Kentucky 40601, within thirty (30) days from the date of this letter. The rules of the Kentucky Board of Tax Appeals, which are set forth in

802 KAR 1:010, require that the complaint or petition of appeal must:

1. Be filed in quintuplicate;

2. Contain a brief statement of the law and laws in issue;

3. State the petitioner's position regarding the law, facts or both; and

4. Include a copy of this final ruling letter with each copy of the complaint or petition.

Proceedings before the Kentucky Board of Tax Appeals are conducted in accordance with 103 KAR 1:010, 802 KAR 1:010 and KRS 131.345-131.365. Formal hearings are held by the Board concerning the tax appeals before it, with all testimony and proceedings officially reported. Legal representation of parties to appeals before the Board is governed by the following rules set forth in Section 2(4) of 802 KAR 1:010:

1. An individual may represent himself in hearings before the Board;

2. An individual who is not an attorney may not represent corporations or individuals before the Board; and

Appendix A

3. An attorney who is not licensed to practice in Kentucky may practice before the Board if he obtains local counsel in compliance with Rule 3.030(2) of the Rules of the Kentucky Supreme Court.

You will be notified by the Clerk of the Board of the date and time set for any hearing.

Sincerely,
s/ George D. Renfro
GEORGE D. RENFRO
Assistant Director
Division of Protest Resolution

APPENDIX B — *CSX CORPORATION AND SUBSIDIARIES VS. DEPARTMENT OF REVENUE* NO. K08-R-37 (KBTA) – ORDER ON MOTION FOR AND MEMO IN SUPPORT OF LIMITING THE KENTUCKY DEPARTMENT OF REVENUE TO FINAL RULING DATED JUNE 3, 2009

COMMONWEALTH OF KENTUCKY
BOARD OF TAX APPEALS
FILE NO. K08-R-37

CSX CORPORATION AND SUBSIDIARIES

APPELLANT

vs.

FINANCE AND ADMINISTRATION CABINET
DEPARTMENT OF REVENUE

APPELLEE

****

This matter is before the Kentucky Board of Tax Appeals to limit the Department of Revenue to its final ruling. Hearings before the board are not limited to previous factual findings and recommendations of the Department or the taxpayer.

Therefore the motion is passed to the merits of the case and may be raised again at the appropriate time.

All other previous orders of the Board remain in effect.

DATE OF ORDER: June 3, 2009

KENTUCKY BOARD OF TAX APPEALS
FULL BOARD CONCURRING.

s/ William A. Hayes
William A. Hayes Chairman

APPENDIX C — ANNUAL STATEMENT ("BLUE BOOK") OF THE COMMONWEALTH LIFE INSURANCE COMPANY OF LOUISVILLE IN THE STATE OF KENTUCKY FOR THE YEAR ENDED DECEMBER 31, 2006 [SELECTED EXCERPTS – COVER PAGE AND PAGE 2 ONLY]

ANNUAL STATEMENT

OF THE

COMMONWEALTH LIFE INSURANCE COMPANY

OF

LOUISVILLE

IN THE STATE OF

KENTUCKY

TO THE

INSURANCE DEPARTMENT

OF THE

STATE OF

FOR THE YEAR ENDED
DECEMBER 31, 1996

1996

LIFE AND ACCIDENT AND HEALTH

1996

Appendix C

ANNUAL STATEMENT FOR THE YEAR 1996 OF THE COMMONWEALTH LIFE INSURANCE COMPANY

ASSETS

	Current Year				Prior Year
	1 Ledger Assets	2 Non-Ledger Assets	3 Assets Not Admitted	4 Net Admitted Assets (Cols. 1+2-3)	5 Net Admitted Assets
1. Bonds (Less $0 liability for asset transfers with o/s options, Schedule B, Part 3)	1,478,671,298	0	0	1,478,671,298	1,348,864,373
2. Stocks					
2.1 Preferred stocks (Schedule D, Part 2, Section 1)	87,288,845	0	0	87,288,845	95,388,722
2.2 Common stocks (Schedule D, Part 2, Section 2)	93,561,645	80,152,661	0	173,714,306	140,545,343
3. Mortgage loans on real estate (Schedule B, Part 1, Section 1)					
3.1 First liens	1,011,740,595	0	0	1,011,740,595	1,041,988,657
3.2 Other than first liens	0	0	0	0	0
4. Real estate (Schedule A, Part 1)					
4.1 Properties occupied by the company (Less $0 encumbrances)	38,699,163	0	0	38,699,163	38,899,110
4.2 Properties acquired in satisfaction of debt (Less ($1,500,000) encumbrances)	9,301,865	0	0	9,301,865	10,167,570
4.3 Investment real estate (Less $0 encumbrances)	135,354	0	0	135,354	632,667
5. Policy loans	172,156,353	0	0	172,156,353	150,893,367
6. Premium notes, including $0 for first year premiums	0	0	0	0	0
7. Collateral loans (Schedule C, Part 1)	0	0	0	0	0
8. Cash ($11,992,300, Schedule E-1) and Short-term investments ($42,617,469, Schedule DA Part 1)	54,609,769	0	0	54,609,769	53,613,960
9. Other invested assets (Schedule BA, Part 1)	169,339,583	0	1,429,933	167,909,650	167,109,893
10. Aggregate write-ins for invested assets	95,977	0	0	95,977	55,222
11. Subtotals, cash and invested assets (Lines 1 to 10)	3,118,955,650	80,152,661	1,429,933	3,196,678,378	3,020,139,858
12. Reinsurance ceded.					
12.1 Amounts recoverable from reinsurers (Schedule S, Part 3)	1,325,384	0	0	1,325,384	2,017,995
12.2 Commissions and expense allowances due	0	0	0	0	0
12.3 Experience rating and other refunds due	0	0	0	0	0
13. Electronic data processing equipment	0	0	0	0	0
14. Federal income tax recoverable	0	0	0	0	0
15. Life insurance premiums and annuity considerations due and uncollected on in force business (less premiums on reinsurance ceded and less $17,115,373 loadings)	0	27,627,881	0	27,627,881	23,237,352
16. Accident and health premiums due and unpaid	0	693,839	11,057	682,582	238,539
17. Investment income due and accrued (Exhibit 3)	0	50,828,124	0	50,828,124	50,997,168
18. Net adjustment in assets and liabilities due to foreign exchange rates	0	0	0	0	0
19. Receivable from parent, subsidiaries and affiliates	6,793,205	0	0	6,793,205	11,348,796
20. Amounts receivable relating to uninsured accident and health plans	0	0	0	0	0
21. Other assets nonadmitted (Exhibit 13)	893,995	0	893,995	0	
22. Aggregate write-ins for other than invested assets	25,113,645	1,461,752	6,066,268	20,508,829	21,313,305
23. Total assets excluding Separate Accounts business (Lines 11 to 22)	3,154,129,880	155,763,057	8,393,993	3,301,498,981	3,129,294,431
24. From Separate Accounts Statement	1,596,179,388			1,596,179,388	1,900,893,935
25. Totals (Lines 23 and 24)	4,750,301,268	155,763,057	8,393,993	4,897,698,791	4,156,388,126
DETAILS OF WRITE-INS					
0901. Financial futures and options	95,977			95,977	55,222
0902.					
0903.					
0996. Summary of remaining write-ins for Line 09 from overflow page	0	0	0	0	0
0999. Totals (Lines 0901 thru 0903 plus 0998) (Line 10 above)	95,977	0	0	95,977	55,222
2201. Miscellaneous admitted assets	966,468	1,339,362		2,305,830	9,111,573
2202. Separate accounts recoverable	6,098,231	142,230	180	7,602,130	9,190,482
2203. CSV Policy Trust	11,190,889			11,190,889	8,198,954
2298. Summary of remaining write-ins for Line 22 from overflow page	6,066,958	0	6,066,958	0	472,745
2299. Totals (Lines 2201 thru 2203 plus 2298) (Line 22 above)	25,113,646	1,461,752	6,066,256	20,508,829	21,313,305

BEST AVAILABLE COPY